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SUBJECT: SPANISH BUDGET NEGOTIATIONS: THE CATALAN POSITION

¶11. Summary: Budget negotiations between the Catalan regional government and the central government will be a key challenge during the budgeting season which begins in earnest this week. The three parties currently in the Catalan government are unified in seeking increased funding for the regional health plan, a long term increase in Catalonia's share of regional government revenue and guarantees of increased infrastructure investment from Madrid. The Catalan government ultimately hopes to obtain a share of the regional budget that more closely reflects its 16% share of the Spanish population and 19% of Spain's GDP, than the roughly 15% it now receives. This money could come either from ceding of more tax monies by the central government or direct transfers from Madrid. The Catalan government believes it is in a strong bargaining position because the Socialist government in Madrid lacks a majority in Parliament and will need the votes of Catalonia's regional parties to pass the 2005 budget by the end of the year. However, the delicate balance between the competing demands of other regional governments and the regional parties in Parliament will be challenging. End Summary.

¶12. Looking ahead to the hard negotiations that will take place between the central government and the autonomous regional governments on their share of Spain's national budget, visiting Madrid Econoff and ConGen Barcelona Pol/Econ Specialist met September 20 with the Catalan regional government's Secretary General of Economy and Finance Martí Carnicer to discuss the Catalan position in the budget debate. The Catalan regional government is one of the regions making the strongest demands for more money from Madrid. Carnicer told us that the three governing parties in the Catalan regional government share the same overall goals of covering the health program deficit, increasing the amount of money received from Madrid, and increasing investment in infrastructure. Carnicer provided a justification of why Catalonia should receive a greater share of the national budget and explained why the current political situation provides the best opportunity for a budgetary reconfiguration in Catalonia's favor.

CURRENT SYSTEM OF FINANCING

¶13. The current financing plan for 15 of the 17 autonomous regional governments is known as the common system and was negotiated in 2001 between the autonomous regional governments and the then ruling Popular Party government. The plan cedes a percentage of taxes collected by the central government in each region to its regional government: 33% of personal income tax, 35% of the value added tax and 40% of the special taxes on alcohol, tobacco and hydrocarbons. Autonomous governments receive 100% of the funds from taxes on property and assets, inheritance, assignments, gambling, vehicle registration and electricity levied within their region. Regional governments also receive a direct transfer called the Sufficiency Fund from the central government budget to the regional governments to cover expenses not met by the tax cessions.

¶14. Under this system, the Catalan government received 12.1 billion Euros (USD 14.8 billion) in revenue in 2002 (the last year with complete budget figures). Tax income provided 84% of Catalonia's revenue and Sufficiency Fund transfers contributed the additional 16% of 2002 revenue. The average regional budget is composed of 68% tax revenue and 32% central government transfers. With this financing system, the Catalan government is expected to have a 2003 deficit of EUR 723 million (USD 887 million) once the accounts are fully reconciled. Roughly EUR 600 million (USD 737 million) of this deficit is from the public health service.

BUDGETARY GOALS OF THE CATALAN GOVERNMENT

¶15. Secretary General Carnicer described the broad goals that the three parties in the Catalan government (Socialist Party of Catalonia--PSC, the Republican Left of Catalonia--ERC and the Initiative for a Green Catalonia--ICV) agree on in the budget negotiation with Madrid. The most pressing issue is obtaining immediate funding for the Catalan public health

program to alleviate its large deficit. In the medium term, the goal is to achieve a revision in the budgetary process that improves Catalonia's long-term revenue. One proposal is to request a greater percentage of taxes collected in Catalonia; the Catalan Counselor for Economy Castells has publicly proposed raising from 35%-40% the amount of value added tax transferred to the autonomous regions. Another option is securing a long-term increase in central government transfers through the Sufficiency Fund or special transfers to cover health care expenses. Finally, all the parties agree on the need for greater central government investment in infrastructure projects in Catalonia, particularly the completion of the high-speed train connection between Madrid and Barcelona and improvements to the Barcelona airport.

16. When asked about how much money the Catalan government was seeking, Carnicer pointed out that 16% of Spain's population lives in Catalonia and that Catalonia produces 19% of Spain's GDP. The three parties therefore expect to receive a percentage of all autonomous government revenue somewhere between those two numbers, rather than the current share of about 15%. We also asked Carnicer about the perception that PSC and ERC might have different goals, considering that the ERC leader Carod-Rovira recently made a personal visit to Madrid to meet with Spanish President Zapatero to push for 19%. Carnicer assured us that there were no key differences between the three parties, though their negotiating tactics might differ and some specific issues might be of greater concern to one party than another. He mentioned that the PSC is focusing on health and infrastructure, and that ERC would like to see increased funding in Catalan language programs.

NOW IS THE TIME

17. Carnicer told us that the Catalan government is in a strong negotiating position, and that the Catalan government believes now is the opportune time to obtain additional funding. He noted that the three-party government is a strong one and willing to fight for its needs during budget negotiations. Catalonia's budgetary goals are agreed on by a large majority of the population and almost 85% of the deputies in the Catalan parliament (the three governing parties plus the former governing party Convergencia i Union). The national government is a "gobierno amigo" or friendly government. The tri-partite Socialist led coalition was elected in November 2003 and the new Socialist led government in Madrid was elected in March 2004. This is the first time in 24 years of Spanish democracy in which both the Catalan regional government and the national government have been of the same party. Friendly atmospherics aside, Carnicer also noted that the national government needed all of the Catalan votes to pass the national budget, as Zapatero governs without an absolute majority. Finally, Carnicer pointed out that the autonomous regions of Catalonia and Andalusia provided many of the votes that allowed the Socialists to take power in Madrid. For all of these reasons, the Catalan parties will push for and expect to receive a change in regional finances that favors Catalonia.

18. Comment: The Catalan government is in a strong position to make demands during the negotiations for the 2005 Spanish Budget. President Zapatero's government does not have a majority in Parliament and will need the Catalan votes to pass his budget. As the first budget of Zapatero's administration, it is likely that the national government will compromise and work hard to pass a budget with a broad range of support by regional parties. Catalonia is probably the autonomous region with the strongest bargaining power due to its size and the alignment of its Socialist-led government with the national government. Catalonia is likely to gain a significant increase in revenue from the budget negotiations. However, the delicate task of balancing Catalonia's increase with demands of other regions in a budgeting environment of high aspirations but fiscal limits will be a major challenge for Zapatero's budget negotiators.

MANZANARES